A meeting of the Board of Governors of the Federal Reserve System with the Federal Advisory Council was held in the offices of the Board of Governors in Washington on Tuesday, September 18, 1951, at 10:30 a.m.

PRESENT: Mr. Szymczak, Chairman pro tem
Mr. Evans
Mr. Norton
Mr. Powell

Mr. Carpenter, Secretary

Messrs. Bucklin, Jackson, Potts, Congdon, Fleming, Davis, Brown, Hemingway, Ringland, Beals, Ray, and Lochead, Members of the Federal Advisory Council from the First, Second, Third, Fourth, Fifth, Sixth, Seventh, Eighth, Ninth, Tenth, Eleventh, and Twelfth Federal Reserve Districts, respectively.

Mr. Prochnow, Secretary of the Federal Advisory Council.

Mr. Szymczak stated that Chairman Martin was absent from Washington attending a meeting of the North Atlantic Treaty Council at Ottawa, Canada, and that Mr. Vardaman was ill.

Before this meeting the Council submitted to the Board of Governors a memorandum setting forth the Council's comments on the subjects to be discussed with the Board at this joint meeting. The statement of the topic, the Council's views, and the discussion with respect to each of the subjects were as follows:

1. Patman Sub-Committee Questionnaires. The Council would appreciate receiving from the Board of Governors copies of the questionnaires submitted to the Board and to the

Federal Reserve Banks by the Patman Subcommittee, and copies of the answers which the Board and the Federal Reserve Banks may make to the questionnaires. If the Board so desires and there is opportunity, the Council would be glad to discuss the answers of the Board to the questionnaire before they are submitted to the Patman Subcommittee.

Mr. Szymczak said that up to the present time the Board had seen only tentative preliminary drafts of the proposed questionnaires to be submitted to the Board and the Federal Reserve Banks, but that the Board would be glad to send copies of the questionnaires to the Council when they were received in final form as well as copies of the answers to the Board questionnaire when they were prepared. Mr. Szymczak also referred briefly to the nature of the questions that might be raised during the sub-committee study. In the ensuing discussion comments were made that, in addition to the questionnaires to be sent to the Board of Governors and the Federal Reserve Banks, questionnaires were also to be sent by the sub-committee to the Treasury, to a number of banks and economists, and possibly others.

2. Prospective Business and Economic Conditions and System Credit Policies. The Board would like to have any views the Council might wish to express on the prospective business and economic situation during the next six months and on the policies that should be followed by the System in the field of general credit controls.

Barring a full-scale war, or a serious lag in the defense program, the Council believes that business during the next six months will be active and will also show a seasonal increase. The demand for credit, partly for seasonal purposes and partly because of the impact of defense production, will markedly increase the volume of bank loans. Under these conditions,

A. The Council believes that bank reserve requirements should not be raised but that a decrease in reserve requirements may be necessary;

B. The Council is opposed to an immediate increase in the rediscount rate, but the situation may change rapidly and the Council may have a different view by the time of its next regular meeting with the Board; and

C. The Council believes that the expected increase in loans plus anticipated deficit financing will probably necessitate providing the banking system with additional reserves either through lower reserve requirements or open market operations. As between these two alternatives, a majority of the Council would favor providing the increased reserves by a reduction in reserve requirements rather than through the Federal Reserve Banks acquiring a large additional amount of Government securities by open market operations. The Council does not believe that under presently anticipated conditions, and with the Voluntary Credit Restraint program in continued operation, a decrease in reserve requirements would accelerate the increase in loans which the Council believes is necessary and inevitable this fall.

President Brown said that the above statement was not intended to mean that the short term rate should be frozen, but that in view of the prospective Treasury deficit any increase in the short term rate beyond 1/8 or 1/4 per cent would be so upsetting to the Government security Market that it would be an undesirable development. Such an increase, he said, should be prevented by open market operations and the discount rate should be kept stable until the situation was clarified. He made the further statement that a seasonal increase in bank loans could not be avoided for the reason that if the banks did not make the loans pressure would be put on Government lending agencies to advance the credit. He added that although the Council was unanimous in its opinion that additional reserve funds would have to be provided, there was a close division of opinion in the Council with a majority feeling that a reduction in reserve requirements would be the preferable means by which reserve funds should be made available. If the amount of needed reserves was small, he said, they could be supplied through open market operations as a more flexible instrument, but the majority of the Council was of the opinion that the amount would be so large that to try to handle it by open market operations alone would increase unduly the amount of securities that the Federal Reserve Banks would have to take.

The problem was discussed in the light of (1) the probable Treasury deficit during the remainder of the calendar year, (2) how the additional funds needed by the Treasury might be raised, having in mind that large amounts of funds for investment in long term issues were not available, and (3) the probable effects of the pending tax bill. It appeared to be the consensus of the Council that the only way the deficit could be financed was in the short term area of the Government securities market.

Statements of Messrs. Jackson and Congdon stressed the desirability of providing additional reserves through a reduction in reserve requirements. Mr. Potts outlined his position that needed reserve funds should be supplied through open market operations, stating that in the very uncertain situation that exists a change as drastic as a reduction in reserve requirements might prove to be too severe and that a smoother operation could be conducted through open market operations. He added that if the situation should change later on and call for more drastic action it could then be taken in the form of a reduction in reserve requirements.

Mr. Szymczak commented on the effects of system credit policies in the current period and on the fact that there were markedly divergent views as to whether inflationary factors would reassert themselves or whether the situation in the months ahead would be one of relative stability. He referred to the statement by Mr. Young, Director of the Board's Division of Research and Statistics, at the meeting of the Council yesterday afternoon in which he gave the reasons for these divergent views, to the problem presented by the Treasury deficit, the existing large inventories, and the effects of increased defense expenditures and the problem created by the uncertainty of how large these expenditures would be. He discussed the elements that would affect the need of the banks for additional reserves during the remainder of the year and how that need could be met effectively by open market operations without indicating a change in credit policy, whereas a change in reserve requirements would be a clumsy instrument the use of which might be regarded as a change in policy. He added that the Open Market Committee and the Treasury were studying the problem of how the Treasury deficit should be financed in the light of the absence of large amounts of medium and long term funds in the market and the desirability of avoiding in an uncertain period like the present becoming committed to a rate by offering a medium or long term issue.

Mr. Fleming suggested that there should be a continuing analysis of the market and available funds for investment in Government securities so that when the time was appropriate for the issuance of long term Government securites, that could be done and the opportunity for such a step would not be lost as it had been at times in the past.

Mr. Jackson stated that the members of the Council who favored a reduction in reserve requirements had not meant to say that open market operations should not be used, but rather that if large amounts of additional reserves were needed they should be supplied through a reduction in reserve requirements.

Mr. Szymczak responded that there appeared to be no conflict in the fundamental views of the Council and the Board, that the difficulty arose out of the fact that no definite formula could be decided upon when the future was as unpredictable as it is at present, and that it would be necessary to watch the situation closely and determine from day to day the actions that should be taken.

3. Changes in the volume of bank loans. What are the prospects with respect to total changes in the volume of bank loans during the rest of the current year?

The Council is unanimously of the opinion that the volume of bank loans will increase during the rest of the current year. An increase in bank loans is inevitable if defense production is to be financed and if the necessary requirements of the economy are to be met.

President Brown commented on this subject in the light of the existing inventory situation and the need for financing defense production and crop movements which presented a clear indication that the volume of bank loans would increase during the remainder of the year. He also said that the banks were experiencing unprecedented demands for loans, that large concerns were asking for increased lines of credit, and that the over-all demand was greater than at any time in the 40 years he had been in the banking business. This demand, he said, apparently would not be materially reduced by an increase of two or three percent in the rate at which the loans were made.

Mr. Szymczak discussed conditions as the Board saw them which would affect the volume of loans and observed that one of the reasons for the current demand probably was the anticipation of further restrictions on the availability of bank credit.

4. Limitation of authority over consumer and real estate credit. In the event strong inflationary pressures should reassert themselves, the limitations imposed by recent legislation on the authorities of the Board over consumer and real estate credit would make it impossible for these authorities to be used effectively

as instruments of selective credit regulation. What would be the recommendations of the Council as to what, if any, recommendations should be made by the Board to the Congress with respect to the removal of the limitations?

The Council on previous occasions has stated, and it still believes, that authority over consumer and real estate credit should not be given to the Board when peacetime conditions prevail. With the existence of a partial war economy, the Council approved granting to the Board, for a limited period, the authority for such selective credit regulations. The Council believes that the imposition by recent legislation of limitations upon the authority previously granted the Board by Congress over consumer and real estate credit was a serious mistake. At an appropriate time the Board should ask for the removal of these limitations.

President Brown stated that the Council felt that with the Congress having recently acted to limit the Board's authority it would be a mistake at any time in the immediate future to request a reversal of the action, and that for that reason the present would not be an appropriate time to make such a request.

Mr. Szymczak referred to the various views with respect to the extent to which selective credit controls should be used in the existing emergency period and to the discussions of whether this instrument might be applied in other fields. He also commented on the use of consumer credit regulation during and since World War II, and the circumstances surrounding the action taken by Congress to limit the authority of the Board in the field of consumer and real estate credit.

Mr. Norton inquired whether members of the Council had had any indication that the recent relaxation of terms on houses under $12,000 would result in a large increase in construction in this price range, and members of the Council responded in the negative.

There was a discussion of the possible volume of construction of higher priced residences, of the indicated overall volume of construction next year, and of the availability of mortgage funds. In connection with the latter point, Mr. Jackson read from a report of interviews with suppliers of mortgage funds in the New York district which indicated that they were following a policy of substantial equity in loans and that it was not likely that they would relax the terms on which mortgage funds would be made available regardless of what the real estate credit regulations might permit them to do.

In response to a further inquiry, Mr. Norton stated that it appeared that the supply of building materials would be adequate except for copper. He also said that the Board had not undertaken to restrict credit for defense housing when the need for such credit had been certified.

There was a general discussion of conditions in the real estate market, the rapidity with which completed houses were being sold, the policies of the Federal National Mortgage Association with respect to the purchase of mortgages, and the funds that insurance companies might have for investment in mortgages in view of other large demands that were being made upon them.

5. Voluntary Credit Restraint Program. What comments does the Council have to make with respect to the

program for voluntary credit restraint and the manner in which it has operated?

At its May meeting with the Board, the Council stated that the Voluntary Credit Restraint Program had met with the general approval not only of banks but also of insurance companies and investment bankers. The program continues to meet with their strong approval. The regional committees throughout the country are now fully organized and functioning. Many loans, aggregating a very large dollar amount, which would not promote either the defense effort or the efficient functioning of the civilian economy, and which without the Voluntary Credit Restraint program would be made, are not being granted by banks or other financial institutions. The knowledge that such loans will be declined has resulted in many would-be borrowers not applying for them.

The Council would like to express again to the Board of Governors, the officials of the Federal Reserve Banks and Governor Powell, who is directly in charge of the program, appreciation for their active and effective efforts to restrictunnecessary and undesirable credit.

The Council recommends more extensive use of literature, news releases, addresses, and other suitable media to bring and keep before lenders and borrowers the objectives of the program.

The Council would like to reemphasize the statement made to the Board in February and again in May of this year, that "Government loans and guaranties of loans in all fields, including real estate, should be terminated, except where such loans are necessary for the defense effort." The present Voluntary Credit Restraint program does not encompass loans guaranteed by the Government or its agencies. The program would be more effective if it included not only private credit, but also loans so guaranteed.

President Brown stated that the banks face real difficulties in refusing credit to credit worthy customers whose business was valuable to the banks, that it was true that loans had been made which were not necessary for the defense effort or the maintenance of necessary civilian activities, but that without the Voluntary Credit Restraint Program many loans would have been made which because of the Program had not been made. As a result, he said, the urge to make loans because of the fear of losing the customer's business to someone else had been greatly reduced, and when large loans were declined for the reason that they were not in harmony with the program there was practically no danger that they would be made by another bank or insurance company. He added that it was remarkable how many people who came into the banks knew about the program, that the danger was that having been launched efforts to keep the program before the public might be relaxed, and that it was desirable to continue to give it the fullest possible publicity and to use every available means such as State Bankers Associations and other meetings of bankers to publicize the program. The Council felt, he said, that Mr. Powell had done an excellent job in "selling" the program.

Referring to the last paragraph of the Council's statement, President Brown said that the Council fully realized the difficulties involved in an effort to restrict Government guaranteed credit and that the Board could not take the initiative in such a move. However, he said, the Council felt that there was a great deal of such credit which should not be made available and if the Voluntary Credit Restraint Program could be applied in that field it would be extremely helpful.

Mr. Fleming said that the reference in the Council's statement to continued publicity for the program had been included because, having just passed through a vacation period, it was necessary to reemphasize the program and its objectives. In that connection, he said, he had spoken to officers of the American Bankers Association, and they had indicated that they also would take steps in the direction of further publicity.

Mr. Powell expressed appreciation of the effective way in which the National Voluntary Credit Restraint Committee and the sub-committees had been working. He said that the success of the program depended largely on continued efforts to keep it and its objective before lending institutions, that the committees had been working effectively "behind the scenes" during the summer, that a meeting of the national committee had been held on September 5 at which time it was decided to step up publicity, that releases had been prepared for that purpose, and that suggestions had been sent to the regional committees for keeping the program before various group meetings so that all publicity would not be coming out of Washington. He made the further statement that there would be a meeting of the chairmen of the regional committees on October 15 at which one of the major topics of discussion would be further steps that should be taken to promote the program and that he would appreciate any suggestions on that point that the members of the Council might wish to make.

In connection with the application of the Voluntary Credit Restraint Program to Government lending agencies, Mr. Powell said that the Wilson four-man committee had fully supported the program, and that an unpublicized report of a committee composed of Messrs. Wilson, Director of Defense Mobilization, Lawton, Director of the Bureau of the Budget, and Keyserling, Chairman of the Council of Economic Advisers, which expressed the view that Government lending agencies should follow policies consistent with the Voluntary Credit Restraint Program, had been sent to all Federal lending agencies as a directive from the President.

Mr. Powell referred to complaints that had been received, particularly from rural areas, that Government lending agencies were not complying with the program, and said that whenever such complaints were received they were taken up promptly with the agency involved and that the agency in each case had asked to be informed of specific cases which appeared not to be in conformity with the program. One complaint, he said, related to the fact that the Government agencies continue to advertise for loans, but it should be kept in mind that private agencies also continue to advertise as part of their business and that the Voluntary Credit Restraint Program could not be carried so far as to put the Government lending agencies out of business. He went on to say that, at the suggestion of the national committee, he had written to each of the Government lending agencies calling attention to the Voluntary Credit

Restraint Program and pointing out how difficult it would be to make the program work if Government lending agencies followed a different policy, and that he had received some very excellent replies that the agencies would comply with the program. Another point, Mr. Powell said, was that the available statistics on the operations of Government lending agencies disclosed that the expansion in their loans was no greater than in the case of private lenders.

Following comments by Mr. Powell relating to the extent to which Government guaranteed mortgage loans might be curtailed, there was a discussion of how far steps in this direction would be desirable. There was also a discussion of the activity of the Federal National Mortgage Association and Mr. Powell stated that the volume of loans acquired by the Association was a very small part of the entire real estate credit picture. Mr. Norton commented that every effort was being made to keep the activities of the Association in line with overall policies with respect to real estate credit.

6. V-Loan Program. Is the V-loan program operating satisfactorily and to what extent is it meeting the need for defense production loans?

Due primarily to slowness in getting action on applications, which delay is not the fault of the Federal Reserve Banks or their staffs, the Council believes the V-loan program is not working as well as was anticipated or as it should.

There was a general discussion of the cause of delays in processing V-Loan applications and how these delays might be avoided. Mr. Szymczak stated that the Board was aware of the situation and would do everything it could to expedite consideration of the applications.

President Brown said that the next meeting of the Council would be held in Washington on November 18-20, 1951.

Mr. Szymczak referred to the procedure under which the Council submits to the Board of Governors before each joint meeting of the Council and Board a memorandum of topics to be discussed at the joint meeting, and stated that before the next meeting the members of the Council might wish to consider whether they would like to make any change in that procedure and whether it would be desirable to provide in the procedure for more informal discussions.

President Brown stated that the Council would be glad to consider the matter.

Thereupon the meeting adjourned.

Secretary.